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Supreme Court of the United States

OCTOBER TERM, 1959.

No. 519

MRS. MILDRED RITTENBERG, WIFE OF AND BERNARD WOHL,
Petitioners and Appellants Below,

versus

UNITED STATES OF AMERICA,
Respondent and Appellee Below.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT.

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HAUSER PRINTING CO., INC., NEW ORLEANS

INDEX

	PAGE
Petition for Writ of Certiorari	1
I. Citation of Opinions Below	1
II. Statement of Jurisdiction	2
III. Questions Presented	2
IV. Statutes Involved	3
V. Statement of the Case and Reasons	3
VI. Reasons Relied on for Allowance of Writ	9
A. An Individual is Allowed as a Deduction in Computing his Net Income all the Ordinary and Necessary Expenses Paid or Incurred During the Taxable Year in Carrying on any Trade or Business.	9
B. An Individual is Allowed as a Deduction in Computing his Net Income all the Necessary Expenses Paid or Incurred During the Taxable Year for the Production or Collection of Income, or for the Management, Conservation, or Maintenance of Property Held for the Production of Income.	21
Conclusion	22
Appendix A	25
Judgment	29
Appendix B	30
Judgment	38
Order Denying Rehearing	38
Appendix C	39

TABLE OF AUTHORITIES

Statutes Cited

PAGE

26 U.S.C. Section 23 (a) (1) (A); Internal Revenue Code of 1939 ..... 2, 3, 7, 9, 22

26 U.S.C. Section 23 (a) (2); Internal Revenue Code of 1939 ..... 2, 3, 7, 21, 33

26 U.S.C. Section 162; Internal Revenue Code of 1954 ..... 2, 3, 7, 9, 22

26 U.S.C. Section 212; Internal Revenue Code of 1954 ..... 2, 3, 7, 21, 22

28 U.S.C. Section 1254 (1) 2

28 U.S.C. Section 1346 8

Cases Cited

Charles J. Dinardo v. Commissioner of Internal Revenue, 22 Tax Court 430 (1954) 15, 22

Deputy v. DuPont, 308 U.S. 488, 84 L. Ed. 416 (1940) 17

Dunn v. McCarthy v. Commissioner, 139 F. 2d 242 (2nd Cir. 1943) 18

United States v. E. J. Bruce Co., Inc., 180 F. 2d 846 (6th Cir. 1950) 12, 22

Wohl v. United States, 267 F. 2d 605 (5th Cir. 1959) 2

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Mrs. Mildred Rittenberg, wife of and Bernard Wohl, petitioners, pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit, entered in the above entitled case on June 16, 1959; rehearing denied August 14, 1959.

I.

CITATION OF OPINION BELOW

The opinion and judgment of the United States District Court for the Eastern District of Louisiana in this matter is not reported but a copy of same is appended hereto.[1]

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[1] Appendix A.

The opinion of the United States Court of Appeals for the Fifth Circuit[2] is reported in 267 F.2d 605 (5th Cir. 1959).

II.
STATEMENT OF JURISDICTION

(1) The decree sought to be reviewed was entered on June 16, 1959.

(2) Application for rehearing was filed on July 27, 1959, and denied on August 14, 1959.

(3) The statutory provision that confers on this Court jurisdiction to review the decree in question; by writ of certiorari, is 28 U.S.C. Sec. 1254 (1).

III.
QUESTIONS PRESENTED

1. Whether rental payments made by a Taxpayer are deductible under Title 26 U.S.C., Section 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C., Section 162 of the 1954 Internal Revenue Code) as ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business when the rental payments made by the Taxpayer are made necessary because F.H.A. regulations prohibit the leasee corporation from making said rental payments and said rental payments are taxpayer's debt and his alone.

2. In the alternative, whether these same rental payments made by a Taxpayer are deductible under Title 26 U.S.C., Section 23 (a) (2) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C., Section 212 of the 1954 Internal Revenue Code) as necessary expenses

[2] Appendix B.

paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income.

IV.

THE STATUTES INVOLVED

This is a suit by Taxpayer asking for a refund of taxes paid by him. Taxpayer claims that he should have been allowed certain deductions in his income tax for the years 1951, 1952, and 1953 under Title 26 U.S.C., Section 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Section 162 of the 1954 Internal Revenue Code) or in the alternative under Title 26 U.S.C. Section 23 (a) (2) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Section 212 of the 1954 Internal Revenue Code). These titles and sections of U.S.C. are set out in Appendix C.

V.

STATEMENT OF THE CASE AND REASONS

In 1949 one of the petitioners herein, Bernard Wohl, began negotiations for the construction and erection of an apartment building on a St. Charles Avenue site in the City of New Orleans, Louisiana.[3] This apartment building was to be constructed in accordance with and under F.H.A. regulations, and therefore, in the same year Mr. Wohl commenced negotiations with the F.H.A. for a commitment to insure a 35 year loan.[4]

F.H.A. required that a corporation be formed to be the builder, owner, operator and mortgagor of the building. A corporation called Wohl, Inc. was then formed

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[3] Tr. pp. 19-20.
[4] Tr. p. 27.

at a nominal capitalization of $1,000.00. Mr. Wohl owned all of the stock in the corporation except for one share which was signed by his wife Mildred Rittenberg and one share which was signed by a secretary.

F.H.A. would have allowed the builder to either purchase a piece of ground or lease a piece of ground upon which to construct the proposed building. The site chosen by Mr. Wohl on which to construct the apartment building was leased ground belonging to Milton Adler and others. Neither Mr. Wohl nor the corporation owned or were to own the land on which the building was to be built.

In preliminary negotiations of which the F.H.A. had full knowledge [5] it was determined that this valuable site on St. Charles Avenue in New Orleans was to be leased under a 99 year lease. Milton Adler, et als, the landowners insisted upon a $12,000.00 rental per year for the first 35 years with renegotiation thereafter. Since F.H.A. regulations prohibited ground rental in excess of a stated percentage of the appraised value of the property, F.H.A. determined that the maximum ground rental could not be in excess of $9,000.00 per year.[6] The Adlers, who were the lessors, would not agree to a ground rental of less than $12,000.00 per year, and in order to comply with F.H.A. regulations, the annual ground rental paid by Wohl; Inc. could not be in excess of $9,000.00.

Mr. Wohl therefore entered into a separate contract with the landowners in which he promised individually to pay $3,000.00 per year for 35 years out of his own funds as rental for the property.[7] F.H.A. had full

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[5] Tr. pp. 20, 23, 28, 31, 34, 49.
[6] Tr. pp. 24-25.
[7] Tr. pp. 23, 24, 35.

knowledge and approved of this action by Mr. Wohl.[8] This obligation on the part of Mr. Wohl was a continuing and recurring one for 35 years and was a personal obligation of Mr. Wohl[9] and was not in any way connected with Wohl, Inc. Mr. Wohl would have preferred that F.H.A. allow Wohl, Inc. to pay the entire $12,000.00 rent,[10] however, under mandatory prohibitions of F.H.A., Wohl, Inc. could pay only $9,000.00 in rent. The payment of the $3,000.00 was Mr. Wohl's debt and his alone.

The Adlers entered into the lease with Wohl, Inc. which lease called for an annual ground rental of $9,000.00 per year for 35 years. The loan insurance was approved by F.H.A. and the apartment building was constructed.

The petitioner herein, Bernard Wohl was and is in the business of managing apartment buildings and apartment units.[11] The majority of Mr. Wohl's income, as reported on his income tax returns, is derived from the business of managing, operating and directing apartment units and houses. Mr. Wohl did not create Wohl, Inc. and build the apartment building on St. Charles Avenue as an investment in the ownership of the apartments or of the stock of Wohl, Inc. Wohl, Inc. was created because F.H.A. required that a corporation be formed to be the builder, owner, operator and mortgagor of the apartment building. Furthermore, Mr. Wohl received no dividends on the Wohl, Inc. stock. Mr. Wohl was interested in one thing only and that was creating additional income to himself and to his wife. Therefore, he incurred this $3,000.00 per year personal obligation so that the apartment building could be built and he could obtain

[8] Tr. pp. 31, 34.
[9] Tr. p. 24.
[10] Tr. p. 24.
[11] Tr. pp. 19-25.

income from the management, operation and direction of the apartment building. Mr. Wohl was and has been the **active manager** of the apartment building since its completion in 1951. As manager Mr. Wohl earned and received a salary of $13,500.00 in 1951, $15,000.00 in 1952 and $13,500 in 1953. During this same period Mr. Wohl was also manager of another apartment building owned by Orleans Park, Inc.[12] in which he was a stockholder. This corporation paid him approximately the same salary for management as did Wohl, Inc.

Counsel for the petitioners wish to again point out to this Honorable Court that under F.H.A. regulations Wohl, Inc. could not pay more than $9,000.00 for the ground rental and under no circumstances could the corporation pay the $12,000.00 asked by the Adlers for the ground rental. Thus, Mr. Wohl entered into a personal obligation to pay the additional $3,000.00 for the ground rental for otherwise he would not have been able to establish his business and pursue his livelihood of managing and operating apartments and would not have been able to derive income as manager of the Wohl Apartments.

In 1951 the apartment building began operation, and during this year Mr. Wohl paid to Milton Adler, et als, under his private agreement and personal obligation the sum of $2,250.00.[13] In 1952 and 1953 Mr. Wohl paid to Milton Adler, et als the sum of $3,000.00 per year under his private agreement and personal obligation.[14] Since the year 1953, petitioner has continued to pay the $3,000.00 per year and will continue to pay this obligation until 1986. Wohl, Inc., in compliance with its agreement with the F.H.A., could not and still cannot assume

[12] Tr. pp. 18-19.
[13] Tr. p. 3.
[14] Tr. p. 3.

any part of this obligation to pay $3,000.00 per year.[15]

The petitioners, within the time prescribed by law, filed with the Director of Internal Revenue at New Orleans, their income tax returns for the years 1951, 1952 and 1953, and thereafter paid the Director of Internal Revenue at New Orleans the income tax assessed upon these returns.[16] The petitioners took as deductions in their income tax in the year 1951 the amount of $2,250.00, in the year 1952 the amount of $3,000.00, and in the year 1953 the amount of $3,000.00. These amounts represented, as mentioned above, the rental payments made by the petitioner Bernard Wohl to the Adlers, et als under his personal obligation and were taken by the petitioners as deductions since they represented ordinary and necessary expenses incurred in carrying on a trade or business under Title 26 U.S.C. Sec. 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Sec. 162 of the 1954 Internal Revenue Code) and in the alternative were taken by the petitioners as an expense incurred in the production of income and conservation of property under Title 26 U.S.C. Sec. 23 (a) (2) of the 1939 Internal Revenue Code as amended (now Title 26 U.S.C. Sec. 212 of the 1954 Internal Revenue Code).[17]

The Director of Internal Revenue disallowed these deductions on the grounds that the petitioners could not claim as a personal deduction the expense of a separate entity and determined therefore that there was a deficiency in the income tax due from the appellants for the calendar years 1951, 1952, and 1953 in the amount of $4,965.04 plus $643.51 as interest upon additional taxes.[18]

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[15] Tr. pp. 54-55.
[16] Tr. p. 3.
[17] Tr. p. 5.
[18] Tr. pp. 3-4.

The petitioners subsequently paid the taxes alleged to be due in the sum of $5,608.55, representing $4,965.04 as taxes and $643.51 as interest.[19] A claim for refund was duly filed and was rejected by the Government, with the following statement:

> "Taxpayers filed claims on August 31, 1955 for additional taxes assessed on 1951, 1952, and 1953 returns. These claims have been given consideration and are recommended for rejection **as taxpayer cannot claim as a personal deduction the expense of a separate entity.** Therefore, they are disallowed as not being 'ordinary and necessary' expenses under provisions of the Internal Revenue Code.
>
> Taxpayers representatives having been informed of his rights to an informal conference stated that conference was not desired." (Emphasis Ours)

It will be noted that the reason for disallowing these deductions was that "taxpayer cannot claim as a personal deduction the expense of a separate entity".

On October 1, 1956, the Commissioner of Internal Revenue notified the petitioners by registered mail of the rejection and disallowance of the aforesaid claim for refund.[20] The petitioners then filed suit in the United States District Court, Eastern District of Louisiana, New Orleans Division asking for a refund of the taxes paid by them.[21] Jurisdiction of the action was vested in that Honorable Court by Title 28 U.S.C. Section 1346, as amended.

On May 16, 1958, trial was held in the District Court in this cause and on September 26, 1958, that Hon-

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[19] Tr. p. 4.
[20] Tr. p. 4.
[21] Tr. pp. 2-6.

orable Court handed down its opinion (Appendix A) granting judgment for the respondent and appellee herein. On October 29, 1958, that Honorable Court handed down its judgment in this cause in favor of the respondent and appellee herein and dismissed the cause of action filed by the petitioners. (Appendix A)

From this judgment the petitioners, Mrs. Mildred Rittenberg, wife of and Bernard Wohl took an appeal to the United States Court of Appeals for the Fifth Circuit.[22] On June 16, 1959, that Honorable Court affirmed the judgment of the District Court (Appendix B) and on August 14, 1959 denied rehearing in this cause. (Appendix B)

VI.

REASONS RELIED ON FOR ALLOWANCE OF WRIT

A.

An Individual Is Allowed As A Deduction In Computing His Net Income All The Ordinary and Necessary Expenses Paid Or Incurred During The Taxable Year In Carrying On Any Trade or Business.

Title 26 U.S.C. Section 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Section 162 of the 1954 Internal Revenue Code) provides as follows:

> " * * * In computing net income there shall be allowed as deductions:
>
> ' * * * all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business * * *; and rentals or other payments required to be made as a con-

[22] T.r. pp. 61, 63.

> dition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity * * *.'"

In order for a taxpayer to take advantage of this section of the Internal Revenue Code he must be engaged in a trade or business and the expense he is deducting must be an ordinary and necessary expense incurred in carrying on the trade or business.

In the case at hand, it is clear that the petitioner, Bernard Wohl, was engaged in the trade or business of managing and operating apartment buildings and apartment units for many years, and the majority of his income, as reported on his income tax returns, was derived from the business of managing, operating and directing apartment units and apartment houses. Since the completion of the apartment building in 1951, the apartments have been entirely managed by Mr. Wohl, and he has devoted his **full time** to the management, running, operating, and hiring of help for these apartments.[23] During this same period of time Mr. Wohl was also the manager of Orleans Park Apartments.[24] He operated these apartments for 11 or 12 years until he sold Orleans Park Apartment, Inc., the corporation which owned the Orleans Park Apartments, in 1954.[25] In its opinion the United States Court of Appeals, Fifth Circuit, states that Mr. Wohl's trade was apartment management.[26]

Wohl, Inc. was formed when it was decided that the apartment building was to be built because F.H.A. **required** that a corporation be formed to be the builder.

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[23] Tr. p. 25.
[24] Tr. pp. 18, 59.
[25] Tr. p. 19.
[26] Appendix B, pg. 33.

owner, operator and mortgagor of the building. Mr. Wohl **was not** chiefly interested in building the apartment building as an investment in the ownership of the apartments or of the stock of the corporation owning them. Mr. Wohl's main interest in building the apartment building was so that he could earn his livelihood by managing it. As already stated he has been the **active** and **full time** manager of the apartments since their completion.

Mr. Wohl owns all but two shares of the stock of Wohl, Inc. One of those two shares of stock is signed by his wife and the other is signed by a secretary.[27] Mr. Wohl has received no dividends from the Wohl, Inc. stock. He did, however, receive a salary from Wohl, Inc. for managing and operating the apartments in the amount of $13,500.00 in 1951, $15,000.00 in 1952 and $13,500.00 in 1953.[28] He also received approximately the same salary from Orleans Park, Inc. and in addition a dividend of $1,650.00 in 1951 and 1952.[29] Certainly, therefor, the payments by Mr. Wohl under his **personal** obligation with the Adlers were not made as an investment in the ownership of the apartments or of the stock of Wohl, Inc. These payments were not capital expenditures and were not investments in the capital of Wohl, Inc. but were made by Mr. Wohl so that he could carry on his trade or occupation as manager of the apartment building, for without these payments personally by Mr. Wohl the apartments could not have been built.

The amounts of $2,250.00 in 1951, $3,000.00 in 1952, and $3,000.00 in 1953, which amounts were paid to the Adlers by virtue of Mr. Wohl's obligation to pay such amounts, were clearly ordinary and necessary expenses

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[27] Tr. p. 28.
[28] Tr. p. 58.
[29] Tr. p. 59.

paid by Mr. Wohl in carrying on his trade or business of managing and operating apartment units and buildings. These payments by Mr. Wohl to the Adlers were made pursuant to his personal obligation with the Adlers to pay $3,000 per year for ground rental.[30] Wohl, Inc. was not a party to the contract under which Mr. Wohl personally obligated himself to pay $3,000.00 per year as rent. Wohl, Inc. was not and could not be legally bound in any way to pay any portion of Mr. Wohl's personal obligation. All that Wohl, Inc. could pay for ground rental under F.H.A. regulations was $9,000.00 per year[31] and that is all Wohl, Inc. contracted to pay. Wohl, Inc. could not and still cannot assume any part of Mr. Wohl's personal obligation to pay the additional ground rental of $3,000.00 demanded by the Adlers. Mr. Wohl would be perfectly willing for Wohl, Inc. to assume his personal obligation but it cannot do so because of F.H.A. regulations.[32] Thus, the payments made by Mr. Wohl to the Adlers by virtue of his personally obligation to them were in no sense of the word business expenses of Wohl, Inc. for they could not possibly be under F.H.A. regulations. **Hence, this is not a case where a stockholder is paying the obligation of the corporation.** These payments were solely the obligation of Mr. Wohl which he had to incur so that the apartments could be built and he could earn a livelihood from managing them.

Counsel for the petitioners feel that the case of *United States v. E. L. Bruce Company, Inc.*[33] is on point in supporting the contention that the payments made by Mr. Wohl by virtue of his personal obligation to the Adlers were ordinary and necessary expenses incurred in his trade or business of managing and operating apart-

[30] Tr. pp. 23, 24, 35.
[31] Tr. pp. 24-25.
[32] Tr. pp. 24, 33.
[33] 180 F. 2d 846 (6th Cir. 1950).

ments. In that case the E. L. Bruce Company entered into a contract with the Terminix Company of Southern California, wherein the E. L. Bruce Company issued a franchise to the Terminix Corporation wherein the Bruce Company would guarantee the effectiveness of the product sold by the Terminix Company. The contract called for an escrow of 7 percent of the amount of each contract entered into between the Terminix Company and the consumer, which sum of money was to be held for the purpose of guaranteeing the customers reinspection and retreatment in the event of the licensee's failure or inability to comply with the terms of the contract. On May 1, 1942, the State revoked the contract of the Terminix Company for failure to fulfill its contracts and the defendant cancelled its license with the Terminix Company. On August 12, 1942, the defendant was granted a license to operate by the State and on August 17, the defendant purchased the physical assets of the Terminix Company. They would not purchase the accounts receivable, cash on hand, and good will but they would sell all rights they had to the escrow agreement. Thereafter the defendant deducted $1,253.09 on unbonded and unguaranteed contracts of the old Terminix Company. The defendant likewise deducted $5,849.31 which was money expended on the bond contracts of the Terminix Company. These deductions were taken as ordinary and necessary business expenses. The Commisisoner of Internal Revenue disallowed these deductions on the grounds that the amounts expended in liquidating the liability of the predecessor were capital expenditures and such were not deductible.

The District Court held in regard to the amount of $1,253.09 as follows:

> "We are of the opinion that the $1,253.09 expended on the unbonded and unguaranteed contracts of the Terminix Company was properly

classified as an ordinary and necessary expense incurred by the taxpayer in carrying on its trade or business. The District Judge found as a fact that **the taxpayer made this expenditure for the protection of its investment and continuance in business: An expenditure for such a purpose clearly falls within the terms of the statute.** *A. Harris & Co. v. Lucas*, 5 Cir., 48 F. 2d 187; *Dunn & McCarthy v. Commissioner*, 2 Cir., 139 F. 2d 242; *Scruggs-Vandervoort-Barney, Inc.*, 7 T.C. 779; *First National Bank of Skowhegan*, 35 B.T.A. 876; *Edward J. Miller*, 37 B.T.A. 830; *Robert Gaylord, Inc.*, 41 B.T.A. 1119. Appellant's contention to the contrary is based upon *Welch v. Helvering*, 290 U.S. 111, 54 S. Ct. 8, 78 L. Ed. 212, where the Supreme Court ruled that the voluntary payment of a taxpayer of unenforceable claims, under conditions there prevailing, was not an ordinary and necessary business expense. In the present case the unbounded contracts of the Terminix Company were not enforceable claims against the taxpayer. The *Welch* case was also relied upon by the Commissioner of Internal Revenue in the *Dunn & McCarthy* case, *supra*, where the Court analyzed and discussed it and pointed out why it was not applicable. It was also distinguished from cases like the present one by the Board of Tax Appeals in *First National Bank of Skowhegan*, *supra*; and in *Edward J. Miller*, *supra*, and by the Tax Court in *Scruggs-Vandervoort-Barney, Inc.*, *supra*. We agree with the rulings in those cases. As there pointed out the expenditures which were disallowed in the *Welch* case were made for the purpose of retaining or protecting an existing good will. **In the present case the District Court's finding that the expenditure was for the protection of the taxpayer's investment is controlling."** (Emphasis Ours)

The Court further held in regard to the expenditures of $5,849.31 as follows:

> "We are also of the opinion that the $5,849.31 expended by the taxpayer on the bonded contracts of the Terminix Company was correctly classified as ordinary and necessary business expense. In addition to the reasons applicable to the nonbonded contract of the Terminix Company, these expenditures were required by its license agreement with the State of California and by its contract obligation with the parent Bruce Company. * * * Such expenses were necessary operating expenses by reason of both the taxpayers license and franchise regardless of the subsequent cumulative provision to that effect in the contract of purchase."

Clearly in this case as in the *Bruce* case *supra* the payments by Mr. Wohl were for the purpose of allowing him to make a living as manager of the Wohl apartments and hence for the protection of his means of making a livelihood.

Counsel feels that the case of *Charles J. Dinardo*,[3] is also in point. In that case the taxpayer was a doctor and a member of a medical partnership consisting of three doctors. The three doctors had previously entered into a non-profit corporation for the purpose of operating a hospital. The doctors had the unrestricted use of the facilities of the hospital and were the only stockholders. During the years 1948 and 1949 the hospital operated at a deficit and the doctors paid the deficit of the hospital corporation and the petitioner deducted his pro-rata portion of the deficit as an ordinary and necessary business expense. The Tax Court held in favor of the taxpayer and against the Commissioner of Internal Revenue and stated on page 436:

> "This case also is distinguishable from *Deputy v. du Pont*, 308 U.S. 488 (40-1 USTC 9161) and

[3] 22 Tax Court 430 (1954).

Eskimo Pie Corporation, 4 T.C. 660 (Dec. 14,348), affd. per curiam 153 Fed. 2d 301 (46-1 USTC 9152), which involve disallowance of a stockholder's deductions for expenditures made on behalf of his corporation, where the corporation's business operations are unrelated to any business the stockholder may carry on other than as a source of investment income.

"Respondent next maintains that the partnership's payment of Collinwood's operating deficits was not an ordinary and necessary business expense. Respondent relies on *Welch v. Helvering*, 290 U.S. 111 (3 USTC 1164). See also *Carl Reimers Co., Inc. v. Commissioner*, 211 Fed. 2d 66 (54-2 USTC 9287), affirming 19 T.C. 1235 Dec. 19,557.

"We disagree with respondent's contentions. The facts in this case more closely resemble the situations involved in decisions which allow, as ordinary and necessary business expenses, payments made by a taxpayer to protect or preserve its business income from loss or diminution. See, for example, *Robert Gaylord, Inc.*, 41 B.T.A. 1149 (Dec. 11,097); *Hennepin Holding Co.*, 23 B.T.A. 119 (Dec. 6938); *First National Bank of Skowhegan*, 35 B.T.A. 876 (Dec. 9626); *Edward J. Miller*, 37 B.T.A. 830 (Dec. 10,024); *Scruggs-Vandervoort-Barney, Inc.*, 7 T.C. 779 (Dec. 15,380); *Dunn & McCarthy v. Commissioner*, 139 Fed. 2d 242 (43-2 USTC 9688), reversing a Memorandum Opinion of this Court entered March 19, 1943 (1 TCM 789, Dec. 13,073M); *Catholic News Publishing Co.*, 10 T.C. 73 (Dec. 16,212); *L. Heller & Son, Inc.*, 12 T.C. 1109 (Dec. 17,053). See also *United States v. E. L. Bruce Co., Inc.*, 180 Fed. 2d 846 (50-1 USTC 9238); *B. Manischewitz*, 10 T.C. 1139 (Dec. 16,458)." (Emphasis Ours)

As can clearly be seen this case cites many cases which the Court states hold that payments by a taxpayer to protect or preserve his business income from loss or

diminution are ordinary and necessary expenses.

Based on the cases above cited, your petitioners believe that the deductions taken by Mr. Wohl and his wife were ordinary and necessary for the production of income by himself and his wife and are properly deductible under Title 26 U.S.C. Section 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Section 162 of the 1954 Internal Revenue Code).

These expenses of Mr. Wohl were in every sense of the word "ordinary" expenses just as much as they were "necessary" expenses of Mr. Wohl for if Mr. Wohl had not obligated himself personally to make the $3,000.00 additional rental payments to the Adlers the apartment building would not have been built and he could not have earned his living from managing and operating these apartments.

This Honorable Court held in the case of *Deputy v. Dupont*[35] as follows:

> "To be sure, an expense may be ordinary though it happened but once in the taxpayer's lifetime. Yet the transaction which gives rise to it must be of common frequent occurrence in the type of business involved. Hence, the fact that a particular expense would be an ordinary or common one in the cause of one business and so deductible under Section 23 (a) does not necessarily make it such in connection with another business."

Surely, the expense incurred by Mr. Wohl in the present suit is not so extraordinary as to occur in the lives of ordinary business men not at all, and in the life of Mr. Wohl but once. Since the completion of the apartment building, Mr. Wohl has continued to pay the $3,-

[35] 308 U.S. 488, 84 L. Ed. 416 (1940).

000.00 per year to the Adlers under his personal obligation and will continue to pay this obligation until 1986.

Furthermore, in the case of *Dunn & McCarthy v. Commissioner*[36] the former President of the taxpayer corporation had borrowed a considerable sum of money from the top ranking salesman of the taxpayer company. Shortly after the loan, the President of the corporation committed suicide and was found to be hopelessly insolvent. The corporation then paid its salesmen the amount of money which had been borrowed by the President on the basis that by doing so they would avoid all ill feeling of the sales personnel and the customers of the corporation. The taxpayer deducted these payments as ordinary and necessary business expenses. The Circuit Court upheld the taxpayer. The Tax Court had previously held that although the payments were necessary they were not ordinary expenses.

> "In the present case the payment was an outlay to retain an existing good will, that is to prevent loss of earnings that might result from destroying good will by failing to recognize the company's moral obligation. Moreover, we do not think that under the circumstances of the present case the expenditure was in a high degree extraordinary. It was the kind of outlay which we believe many corporations would make and have made under similar circumstances. * * * The situation may be unique in the life of the petitioner, but it is not so in the life of business corporations as a group."

Possibly, no other person engaged professionally in the personal service business of apartment management make payments of the kind made by Mr. Wohl in the case at hand. Yet, possibly there are no other, or very

[36] 139 F. 2d 242 (2nd Cir. 1943).

few, situations as we have here where, in order that he might earn a livelihood, a taxpayer has to bind himself personally to make certain payments which a corporation, he is required to form because of government regulations, cannot make because of government regulations. Does this mean that these expenses would not be ordinary to such a business if another situation like this arose? It is felt that any businessman would certainly make such payments in order to provide himself with employment. This is a very similar situation as that of a lawyer paying rent for an office in order to practice law.

These expenses of Mr. Wohl were clearly "necessary" if he was to earn his living from managing these apartments. These expenses were certainly "necessary" for the purpose of expanding Mr. Wohl's employment in a current occupation. As already pointed out Mr. Wohl has been for many years in the business of managing and operating apartment buildings. If he had not personally obligated himself to make these additional rental payments, then under F.H.A. regulations the apartment building would not have been built and most certainly Mr. Wohl would not have become the manager. Mr. Wohl was for all practical purposes the sole stockholder of Wohl, Inc. and received no dividends on its stock. True, Mr. Wohl had no long-term employment contract with Wohl, Inc. Yet, if he did not bind himself to make the $3,000.00 rental payments personally he could not have ever become the manager of these apartments for they never would have come into existence at all.

Counsel for the petitioners wish to again point out to this Honorable Court that the payments of Mr. Wohl to the Adlers were clearly not capital expenditures and were not investments in the capital of Wohl, Inc. F.H.A. required that Wohl, Inc. be formed. Mr. Wohl owns, for

all practical purposes, all of the stock in Wohl, Inc. Mr. Wohl has received no dividends on this stock. He has received a substantial salary each year for the managing of the apartments and has been the active and full time manager of the apartments since their completion. Wohl, Inc.'s obligation for rental was $9,000.00. It paid that. Under mandatory prohibitions of F.H.A. it could pay no more. Wohl, Inc. has no obligation to pay the $3,000.00 each year for rental and it is solely the obligation of Mr. Wohl and his debt alone. There are many cases in the jurisprudence where a stockholder pays an obligation of the corporation merely to obtain maximum tax benefit to himself. This is not true in this case since Mr. Wohl could not legally obligate Wohl, Inc. to make these payments. Thus, this is not a case where a stockholder is paying the obligation of the corporation.

Mr. Wohl decided to incur this obligation so that he could derive additional income as the manager of the apartments. In this matter, Mr. Wohl derives income as an operating manager of the apartments. The petitioners would be prefectly willing for Wohl, Inc. to assume the obligation of Mr. Wohl, and the corporation would be perfectly willing to assume this obligation but it is prohibited from doing so by virtue of F.H.A. regulations.

In summary, counsel for the petitioners feel that they have shown that Mr. Wohl was engaged in the trade or business of managing and operating apartment buildings, and that the expenditures made by him in 1951, 1952 and 1953 in the respective amounts of $2,250.00, $3,000.00, and $3.000.00 were ordinary and necessary expenses incurred by him personally in order that he might carry on his business of managing apartment buildings and thus afford himself an opportunity to make a living.

B.

An Individual Is Allowed As A Deduction In Computing His Net Income All Of The Necessary Expenses Paid Or Incurred During The Taxable Year For The Production Or Collection Of Income, Or For The Management, Conservation, Or Maintenance Of Property Held For The Production of Income.

Title 26 U.S.C. Section 23 (a) (2) of the 1939 Internal Revenue Code as amended (now Title 26 U.S.C. Section 212 of the 1954 Internal Revenue Code) provides as follows:

> " * * * In the case of an individual all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income."

If this Honorable Court should find that the petitioner Bernard Wohl, was not engaged in the trade or business of managing and operating apartment buildings, then in the alternative this Honorable Court should hold that the expenditures made by Mr. Wohl fall within the deductions allowed by Title 26 U.S.C. Section 23 (a) (2) of the 1939 Internal Revenue Code as amended.

The expenditures made by Mr. Wohl as already pointed out were certainly "ordinary" and "necessary" for without them the apartments would not have been built and Mr. Wohl could not have made a living by managing them. Mr. Wohl in making these expenditures was not trying to create any new trade or business. He made these expenditures so that he might continue his existing business and continue earning his livelihood by managing apartments as already pointed out. Mr. Wohl had been for many years engaged in the trade or business of managing apartments. Hence, these payments by

Mr. Wohl were certainly made for the production of income[37] and were certainly made for the protection and continuance of his business. Counsel feels that the cases of *United States v. E. L. Bruce Company, Inc.*[38] *supra* and *Charles J. Dinardo*[39] *supra* support this position.

CONCLUSION

In conclusion, your petitioners, Mrs. Mildred Rittenberg, wife and/or Bernard Wohl, respectfully submit that Bernard Wohl was in the trade or business of managing and operating apartment buildings and that the amounts paid by Mr. Wohl to the Adlers of $2,250.00 in 1951, $3,000.00 in 1952 and $3,000.00 in 1953 were "ordinary and necessary" expenses of his trade or business and therefore should have been allowed as deductions on the petitioners' income tax returns for those years under Title 26 U.S.C. 23 (a) (1) (A) of the Internal Revenue Code of 1939 as amended (now Title 26 U.S.C. Section 162 of the 1954 Internal Revenue Code).

In the alternative, if this Honorable Court should find that Mr. Wohl was not in the trade or business of managing apartment buildings then these amounts should have been allowed as deductions under Title 26 U.S.C. Section 23 (a) (2) of the 1939 Internal Revenue Code as amended (now Title 26 U.S.C. Section 212 of the 1954 Internal Revenue Code).

Petitioners further respectfully submit that these amounts should not have been disallowed by the Commissioner on the grounds that the "taxpayer cannot claim as a personal deduction the expense of a separate entity."

The amounts paid by Mr. Wohl were paid by virtue of his personal agreement with the Adlers. As pointed

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[37] Tr. p. 35.
[38] 180 F. 2d 846 (6th Cir. 1950).
[39] 22 Tax Court 430 (1954).

out, Wohl, Inc. was not a party to this agreement and did not and could not legally assume any part of the obligation because of F.H.A. regulations. Hence, these payments by Mr. Wohl were not in any sense of the word expenses of the corporation. Mr. Wohl was forced by government regulation to personally make these payments in order that he might continue his business of managing and operating apartments and thus continue to earn his livelihood.

In the event the petitioners are not entitled to a deduction for the amounts paid by them each year, so that Bernard Wohl may receive income upon which he pays an income tax, a most inequitable result would prevail. It is felt that such a situation should never be permitted.

Petitioners respectfully submit that the United States Court of Appeals for the Fifth Circuit, in the respects above mentioned, erred in affirming the decision of the District Court in this matter and these errors are so prejudicial to the petitioners as to call for the exercise of this Court's power of supervision by Writ of Certiorari.

Respectfully submitted,

ROBERT WEINSTEIN,
624 Whitney Building,
New Orleans, Louisiana,
Attorney for Mrs. Mildred Rittenberg, Wife of and Bernard Wohl, Petitioners and Appellants Below.

SYLVAN J. STEINBERG,
JOHN A. SHANKS,
of
RITTENBERG, WEINSTEIN & BRONFIN,
624 Whitney Building,
New Orleans, Louisiana,
Of Counsel.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Petition for Writ of Certiorari and the Appendices that follow have been served on the Solicitor General, Department of Justice, Washington 25, D. C.; the Honorable Charles K. Rice, Assistant Attorney General, Department of Justice, Washington 25, D. C.; the Honorable Lee A. Jackson and Carter Bleadsoe, Attorneys, Department of Justice, Washington 25, D. C.; the Honorable M. Hepburn Many, U. S. Attorney, Federal Building, New Orleans, Louisiana, and the Honorable Prim B. Smith, Jr., Assistant U. S. Attorney, Federal Building, New Orleans, Louisiana by placing same in the United States mail with first-class postage prepaid, addressed to the above Counsel of Record at their Post Office Addresses.

New Orleans, Louisiana, November , 1959.

APPENDIX A

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF LOUISIANA
NEW ORLEANS DIVISION

CIVIL ACTION
NO. 6712

MRS. MILDRED RITTENBERG, Wife of,
and BERNARD WOHL,
Plaintiffs,

versus

UNITED STATES OF AMERICA,
Defendant.

WRIGHT District Judge:

This suit involves the disallowance of certain deductions claimed by the plaintiff as business expenses in his federal income tax returns for the years 1951, 1952 and 1953.

In 1949 the taxpayer was negotiating with the Federal Housing Administration for insurance of a 35-year loan which was to finance the construction of an apartment building. A corporation, called Wohl, Inc., was to be formed to carry out the project and own and manage the apartments. The owners of the lot on which the building was to be constructed refused to lease it at less than $12,000 per year, but the FHA would not insure the loan if the ground rental exceeded $9,000 per year. Whereupon taxpayer entered into a separate contract with the landowners in which the taxpayer promised to

pay the landowners $3,000 per year, for 35 years out of his own funds in return for their agreement to lease the land for 99 years to Wohl, Inc., at $9,000 per year for the first 35 years.

Immediately thereafter, Wohl, Inc. was formed, with taxpayer as its principal promoter, officer and stockholder. The landowners signed the lease with Wohl, Inc., the loan insurance was approved by the FHA, and the building was constructed. Taxpayer is now the sole stockholder of Wohl, Inc., and has been the manager of the apartment building since its completion in 1951. As such, he received a salary of $13,500 in 1951, $15,000 in 1952, and $13,500 in 1953. He has received no dividends on his Wohl, Inc. stock. During the period in suit, taxpayer was also manager of another apartment building owned by Orleans Park, Inc., of which he was also a stockholder. Orleans Park, Inc. paid him approximately the same salary as Wohl, Inc., and, in addition, a dividend of $1,650 in 1951 and 1952.

Under the private agreement made to secure the lease for Wohl, Inc., taxpayer paid the landowner $2,500 in 1951, $3,000 in 1952 and 1953, and deducted these sums from his gross income as "ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business."[1] The Commissioner disallowed these deductions on the theory that they were properly the business expense of Wohl, Inc., and not of the taxpayer, and that they should be treated as capital contributions to the corporation. Taxpayer contends that these payments are his deductible expenses under Section 23(a)(1) and (2) of the 1939 Code.

The facts will not support the premise that the pay-

[1] Internal Revenue Code of 1939, Section 23(a)(1)(A); 26 U.S.C. § 23 (1952 ed.).

ments in suit are business expenses of Wohl, Inc. The obligation in question is entirely separate from the business of Wohl, Inc. Although both parties, and the agreement itself, refer to the payments of $3,000 per year as "additional rentals," this is a misnomer. Wohl, Inc. is in no way liable for, and cannot under FHA regulations assume, this personal obligation of the taxpayer. Wohl, Inc. was not a party to this agreement, and its leasehold would be unafected by taxpayer's failure to make his yearly payments. This is not to say that Wohl, Inc., did not benefit from taxpayer's contract with the landowner. It obviously did. But that fact did not any more obligate Wohl, Inc., on that contract than any corporation is obligated to retire a bank loan made by one of its stockholders to pay the corporation for the purchase of his stock. Actually, the contract in suit was a capital contribution to Wohl, Inc., a corporation now wholly owned by the taxpayer. It was a strategem to circumvent the FHA regulations.

Taxpayer asserts that he is in the business of "managing and operating apartment houses" and that this contract obligation was and is an ordinary and necessary expense of carrying on that business. If, by "business" he means his salaried employment as manager of Wohl, Inc., this contention must fail since he can carry on as manager whether the payments are made or not. If the taxpayer's business is defined more broadly to include his activities as promoter and officer of Wohl, Inc.,[2] it is nevertheless apparent that the incurring of this obligation was only a condition precedent to the inauguration of that enterprise and is now independent of it. Should taxpayer retire as manager, and as an officer of Wohl, Inc., and transfer all his stock, this personal obli-

[2] Cf. *Foss v. Commissioner of Internal Revenue*, 1 Cir., 75 F. 2d 326.

gation would nonetheless continue.

On either definition of taxpayer's business, this contract obligation was necessarily incurred in order to create the business. As such, it is in the nature of a capital contribution and the payments thereunder are not deductible as a current business expense. *Alexander M. Bing*, 30 B.T.A. 429, aff'd. 2 Cir., 76 F. 2d 941; *Isabelle Hammond-Knowlton*, 19 B.T.A. 947. Cf. *Cooper Foundation v. O'Malley*, 8 Cir., 221 F. 2d 279; *Nachman v. Commissioner of Internal Revenue*, 5 Cir., 191 F. 2d 934; *King Amusement Co. v. Commissioner of Internal Revenue*, 6 Cir., 44 F. 2d 709. See also *Southwestern Hotel Co. v. United States*, 5 Cir., 115 F. 2d 686; 4 Mertens, Federal Income Taxation §§ 25.27, 25.35, 25.40.

Judgment for defendant.

s J. SKELLY WRIGHT
UNITED STATES DISTRICT JUDGE

New Orleans, Louisiana
September 26, 1958

CLERK'S COPY
A True Copy
Oct. 2, 1958

s EVERETT REGNOR
Deputy Clerk, United States District Court
Eastern District of Louisiana
New Orleans, La.

[SEAL]

IN THE
UNITED STATES DISTRICT COURT FOR THE
EASTERN DISTRICT OF LOUISIANA
NEW ORLEANS DIVISION

CIVIL ACTION
NO. 6712

MRS. MILDRED RITTENBERG, Wife of,
and BERNARD WOHL,

Plaintiffs,

versus

UNITED STATES OF AMERICA,

Defendant.

J U D G M E N T

This cause having been submitted to the Court at a former date, by counsel for the respective parties, on the pleadings, exhibits, stipulation, testimony adduced at the trial, and the briefs of the parties;

And the Court having heretofore rendered an opinion which serves as its Findings of Fact and Conclusions of Law, and being fully advised,

IT IS NOW ORDERED AND ADJUDGED by the Court that judgment be and is hereby entered in favor of the defendant, United States of America, and against the plaintiffs, Mrs. Mildred Rittenberg, Wife of, and Bernard Wohl, and that plaintiffs' cause of action be and it is hereby dismissed. The costs of this action shall be paid by plaintiffs, for which judgment is rendered and execution thereon awarded.

APPENDIX B

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 17673

MRS. MILDRED RITTENBERG, wife of
and BERNARD WOHL,
Appellants,

versus

UNITED STATES OF AMERICA,
Appellee.

Appeal from the United States District Court for the Eastern District of Louisiana.

(June 16, 1959.)

Before HUTCHESON, Chief Judge, and BROWN and WISDOM, Circuit Judges.

BROWN, Circuit Judge: The question here, as in so many tax cases, is whether the expenditures by Taxpayer were deductible either as a Section 23(a)(1)(A) "ordinary and necessary" business expense or a Section 23(a)(2) "ordinary and necessary" non-business expense paid for the production or collection of income. Internal Revenue Code 1939, Setcion 23, 26 USCA.

The expenditure for the three years involved was in reality a payment of a part of the ground rental to owners of the land on which Taxpayer's wholly owned corporation, Wohl, Inc., had built a modern multi-story

apartment building, the Wohl Apartments with the aid of an FHA guaranteed mortgage loan of $2,300,000.

In 1949 Taxpayer commenced negotiations with the Federal Housing Administration for a commitment to insure a 35-year loan. FHA required that a corporation be formed to be the builder, owner, operator and mortgagor of the building. The corporation was formed at a nominal capitalization of $1,000. Neither Taxpayer nor his corporation owned or were to own the land on which the building was to be built. This valuable site on St. Charles Avenue in New Orleans was to be leased under a 99-year lease. The landowners insisted upon a $12,000 rental per year for the first 35 years with renegotiation thereafter. Under FHA regulations which prohibited ground rental in excess of a stated percentage of the appraised value, the maximum rental was $9,000 per year. The landowners insisted upon $12,000 rental per year. FHA was unswerving in its ceiling of $9,000 per year.

With the acquiescence if not tacit approval of FHA, Taxpayer entered into a separate contract with the landowners in which he promised individually to pay $3,000 per year for 35 years out of his own funds in return for the landowner's agreement to lease the land to the corporation, Wohl, Inc., for 99 years at $9,000 per year for the first 35 years.

The landowners signed the lease with Wohl, Inc., the loan insurance was approved by FHA, and the building was constructed. Pursuant to this personal agreement, Taxpayer paid the landowners $2,250 in 1951, $3,000 in 1952, and $3,000 in 1953. He deducted these sums from his personal gross income as ordinary and necessary business expenses.

In addition to being the sole stockholder of Wohl,

Inc., Taxpayer has been the active manager of the apartment since its completion in 1951. As manager, he earned and received a salary of $13,500 in 1951, $15,000 in 1952 and $13,500 in 1953. Taxpayer received no dividends on the Wohl, Inc. stock. During the same period Taxpayer was also manager of another apartment building owned by Orleans Park, Inc. in which he was a stockholder. This corporation paid him approximately the same salary for management as did Wohl, Inc.

The Commissioner disallowed these deductions on the theory that they were properly the business expenses of Wohl, Inc., the corporation, and not those of Taxpayer, and that they should be treated as capital contributions to the corporation. The District Court after a nonjury trial which included some oral testimony concerning the circumstances and purpose of the supplemental agreement to pay rent as well as many documents, likewise held against Taxpayer. We agree.

Taxpayer's theory is that his regular trade and business was that of the management of apartments. Therefore, he insists, the agreement to make the supplemental rental payments with the landowners was to enable him to get a contract which would pay him a substantial salary as manager of the apartment when and as built. He does not claim that he was in the regular business of paying rentals for properties owned either by his own corporations or by other corporations. And he vehemently disavows the purpose attributed to him by the Commissioner of claiming as a personal deduction the expense of the separate corporate entity.[1] The corporation's obliga-

[1] The claim for refund filed administratively prior to suit was rejected with the following statement by the Commissioner's representative. "These claims have been given consideration and are recommended for rejection as *taxpayer cannot claim as a personal deduction the expense of a separate entity.* Therefore, they are disallowed as not being 'ordinary' and necessary' expenses under the provisions of the Internal Revenue Code * * *." (emphasis supplied)

tion for rental was $9,000. It paid that. Under mandatory prohibitions of FHA it could pay no more. The payment of the $3,000 was Taxpayer's debt and his alone.

What Taxpayer does not contend is significant. For it highlights the necessity of his demonstrating that this annual payment was (a) an expense of the personal service business of apartment management, and as such was (b) necessary and (c) ordinary.

On factor (a), the business of apartment management, we can assume, as does the Government, that this was his trade. Such an assumption, however, does not discard the remainder of the uncontradicted testimony showing that he was, in his own words, engaged "exclusively in *building* and managing apartments," which means investment in the ownership of apartments or of stock of corporations owning them. And while explaining that he made the personal supplemental agreement to pay $3,000 a year since this was "the only way that I could have established this business and kept myself employed and made a livelihood * * *," he reflects categorically another major purpose. "This was my investment, personally, to build this building. Without such an added investment I could not have built this building on this particular piece of ground."

Factors (b) and (c)—ordinary and necessary—unavoidably justify the conclusion that "despite the multitude of decisions involving interpretations of that term, each case must still be determined on the basis of its peculiar facts and circumstances." 4 Mertens, Law of Federal Income Taxation, § 25.09 at 19 (1954). And in this case by case search, we are reminded that the decisive distinctions are those of degree and not of kind. To this the Supreme Court added, there is no "verbal formula that will supply a ready touchstone" since the statutory

standard "is not a rule of law: it is rather a way of life. Life in all its fullness must supply the answer to the riddle." *Welsh v. Helvering*, 1933, 290 U.S. 111, 115, 54 S. Ct. 8, 78 L. Ed. 212.

Little would be served in trying to recatalogue the inner and outer reaches of necessary and ordinary, or to delineate those factors whose presence or absence leads to one rather than the other conclusion. See *Deputy v. du Pont*, 1940, 308 U.S. 488, __ S. Ct. __, 84 L. Ed. 416; *Welsh v. Helvering*, *supra*; and 4 Mertens, *supra*, §§ 25.05-25.09. How, if any, may be considered as decisive. It is sufficient, we think, briefly to indicate some facets of this record which support the conclusion both of fact and law of the District Court that these supplemental rental payments were not ordinary and necessary expenditures made in the course of the personal service business of managing apartments.

There is, first, nothing in the record to compel the factual-legal conclusion that the payment was made, as Taxpayer now claims, to get him a lucrative job as manager of his own apartment even if that is assumed to be sufficient. This might have been one of its purposes but the Trial Court was entitled to think, as he presumably did, that this was far overshadowed both in purpose and necessity by other factors. The prospective job as apartment manager was quite remote in the chain of consequences. There were a number of steps before that employment came into fruition and as to each of them the personal agreement to pay the supplemental rent was an essential prerequisite. Without the land the apartment could not be built. Without the lease the land could not be acquired. Without the loan the apartment could not be built. Without the FHA commitment the loan could not be obtained. Without the reduction of rental payable by

the corporation to $9,000 the commitment could not be secured. Without the personal agreement to supplement the rent by $3,000 none could be obtained. Conversely, by paying the $3,000 Taxpayer got much more than prospective employment. He would become the beneficial owner of an apartment costing in the neighborhood of $2,300,000 which would be paid out in the 35-year term of the mortgage which coincided with the term of the supplemental agreement.

Looking at is from these directions, the expenditure cannot be described as predominantly for the purpose of expanding employment in a current occupation. The use of a corporation to build, own and operate the apartment was a requirement of the FHA. The salary could continue only so long as the operation produced enough revenues over and above amortization of the debt and the cost of operations excluding the owner-manager's salary. If operations did supply such revenues with which to pay the manager's salary, the corporate owner (and hence Taxpayer's) equity in the building was automatically increasing.

From this same vantage point what is paid hardly seems to have been ordinary as that term is used, not in its ordinary sense, but in the extraordinary sense of this ordinary expense tax exemption. Granted, as one authority puts it, that the test of what is ordinary may be that of the "hard-headed businessman," 4 Mertens, *supra*, §25.09 at 25, which allows the deduction if "the average hard-headed businessman" might have made the expenditure, although its payment seems unusual or unique or doubtful to one not having the responsibilities of management, we do not think this payment meets even this flexible standard.

There was no proof that persons engaged profession-

ally in the personal service business of apartment management make payments of the kind or amount even remotely resembling this supplemental rent. The obligation to pay the supplement ran for 35 years. It was in no way related to continuation of Taxpayer in the management, or the possibility that, in this world of vicissitudes, accidents, epidemics and disabling diseases, Taxpayer might not, at some unknown time, become unable to perform this work. Indeed, so far as this record goes, there was not even assurance that a management contract would continue for the life of the supplemental payment, the life of the Taxpayer, or the life of the mortgage. So long as things went well, presumably Taxpayer could control his corporation to secure continuation of the employment. But if things went bad, or revenues were inadequate or default was actual or imminent so that outsiders might have a legal ground for interest in the internal affairs of the corporation, the corporation was not bound to Taxpayer under any long-term employment contract.

That this payment cannot readily be pegged in any traditional category is of no consequence. "If this results in making the item a nondescript before the law or puts it in a vacuum abhorrent to the accountant, so it must stand." Connally Realty Co., 31 B.T.A. 349, 350, aff'd 1936, 5 Cir., 81 F. 2d 221. It is rental to the landowner at least and hence an operating expense of a kind which the corporation would ordinarily pay and which all, save the FHA, desired the corporation to pay. It was a capital expenditure in the sense that it was an indispensable payment for Taxpayer either to get ownership of an expanding equity in a valuable building, to get the building at all, or a chance to work. From the corporation's viewpoint it was, in a sense, as though Taxpayer had delivered to the corporation an undivided one-fourth leasehold (annual rental $12,000 of which $3,000 was to be

paid by him). Its hybrid character is but one of the unique consequences which occur in this complex life as tax law, the Commissioner of Internal Revenue, the FHA and its administrative practices, the separate entity of the wholly owned corporation of nominal capitalization and the Taxpayer all converge in this apartment building enterprise.

We do not think that *United States v. E. L. Bruce Co.*, 6 Cir., 1951, 180 F. 2d 846; Charles J. Dinardo, 22 T.C. 430 (1954); *Dunn & McCarthy, Inc. v. Commissioner*, 2 Cir., 1943, 139 F. 2d 242, so heavily pressed by Taxpayer require a different result. These expenditures were not, as were those, for the protection of an existing investment or the continuance of an existing business, or the preservation of existing income from loss or diminution. Here it was to acquire an investment, to obtain a new job, to secure new income that caused the personal agreement to be made.

For like reasons, the effort to come under Section 23(a)(2) as a nonbusiness expense is equally unsuccessful.

AFFIRMED.

A true copy

Test: EDWARD W. WADSWOTH
Clerk, U. S. Court of Appeals,
Fifth Circuit

By s/ GILBERT F. GAMCHEAU
Deputy

New Orleans, Louisiana
Oct. 19, 1959

[SEAL]

JUDGMENT

Extract from the Minutes of June 16, 1959

MRS. MILDRED RITTENBERG, wife of,
and BERNARD WOHL,

No. 17673. *versus*

UNITED STATES OF AMERICA.

This cause came on to be heard on the transcript of the record from the United States District Court for the Eastern District of Louisiana, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be, and the same is hereby, Affirmed.

ORDER DENYING REHEARING

Extract from the Minutes of August 14, 1959.

MRS. MILDRED RITTENBERG, wife of,
and BERNARD WOHL,

No. 17673. *versus*

UNITED STATES OF AMERICA.

It is ordered by the Court that the petition for rehearing filed in this cause be, and the same is hereby, denied.

APPENDIX C

TITLE 26 U.S.C.
INTERNAL REVENUE CODE OF 1939 AS AMENDED

Section 23. **"Deductions from gross income.** In computing net income there shall be allowed as deductions:

(a) **Expenses.**

(1) **Trade or business expenses.**

(A) **In general.** All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity. In the case of any sports program conducted for the benefit of the American National Red Cross, expenses described in sections 22 (b) (16) (B) shall be allowable under this subparagraph only to the extent that such expenses exceed the amount excluded from gross income by section 22 (b) (16)."

* * * * *

(2) **"Non-trade or non-business expenses.** In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income."

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Office-Supreme Court, U.
FILED
DEC 4 1959
JAMES R. BROWNING, C

No. 519

In the Supreme Court of the United States

OCTOBER TERM, 1959

MILDRED RITTENBERG AND BERNARD WOHL, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

J. LEE RANKIN,
Solicitor General,
CHARLES K. RICE,
Assistant Attorney General,
ROBERT N. ANDERSON,
CARTER BLEDSOE,
Attorneys,
Department of Justice, Washington 25, D.C.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	2
Argument	3
Conclusion	5
Appendix	6

CITATIONS

Cases:

Deputy v. *duPont*, 308 U.S. 488 ... 5

Dinardo v. *Commissioner*, 22 T.C. 430 ... 5

Dunn & McCarthy v. *Commissioner*, 139 F. 2d 242 ... 5

Frank v. *Commissioner*, 20 T.C. 511 ... 4

Hammond-Knowlton v. *Commissioner*, 19 B.T.A. 947 ... 4

Low v. *Nunan*, 154 F. 2d 261 ... 5

McDonald v. *Commissioner*, 323 U.S. 57 ... 4

Peto v. *Commissioner*, decided February 28, 1958, affirmed *per curiam*, 262 F. 2d 342 ... 4

United States v. *E. L. Bruce Co.*, 180 F. 2d 846 ... 5

Welch v. *Helvering*, 290 U.S. 111 ... 5

Statute:

Internal Revenue Code of 1939, Sec. 23(a) (26 U.S.C. 1952 ed. 23(a)) ... 2

In the Supreme Court of the United States

OCTOBER TERM, 1959

No. 519

MILDRED RITTENBERG AND BERNARD WOHL, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 57–61) has not been reported. The opinion of the Court of Appeals (Pet. 30–37) is reported at 267 F. 2d 605.

JURISDICTION

The judgment of the Court of Appeals was entered on June 16, 1959 (Pet. 38). A petition for rehearing was denied on August 14, 1959 (Pet. 38). The petition for writ of certiorari was filed on November 6, 1959. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether annual payments made by a taxpayer to supplement rentals paid by a corporation owned by him in order to permit the corporation to build, and himself to manage, an apartment building, were deductible by him as ordinary and necessary business expenses or as non-business expenses.

STATUTE INVOLVED

Section 23(a) of the Internal Revenue Code of 1939 is set forth in the Appendix, *infra*, p. 6.

STATEMENT

In 1949 the taxpayer[1] entered into negotiations with the Federal Housing Administration for a commitment to insure a thirty-five-year loan which was to finance the construction of an apartment building, costing approximately $2,300,000 (Pet. 31, 35; R. 58). A corporation, wholly owned by the taxpayer, called Wohl, Inc., was formed to carry out the project and to own and manage the apartments (R. 58). One of the conditions of the F.H.A. commitment was that the ground rental to be paid by the corporation for the land upon which the building was to be erected would not exceed $9,000 per year. The land owners requested $12,000 rental per year for the ground and, in order to overcome this difficulty, the taxpayer entered into a separate contract with the land owners whereby he promised to pay $3,000 per year for thirty-five years out of his own funds in return for the land owners' agreement to lease the land for ninety-nine

[1] The taxpayers were man and wife, the husband being the party personally involved in the transactions described.

years to Wohl, Inc., at $9,000 per year for the first thirty-five years (Pet. 31, R. 58).

The land owners signed the lease with Wohl, Inc., the loan insurance was approved by the F.H.A., and the building was constructed. The taxpayer has been manager of the apartment building at a salary of from $13,500 to $15,000 a year since its completion in 1951. During the period in suit, the taxpayer was also manager of another apartment building owned by another corporation in which he was a stockholder (Pet. 31–32, R. 58–59). Under the private agreement made to secure the lease for Wohl, Inc., the taxpayer paid the land owners $2,250 in 1951, $3,000 in 1952, and $3,000 in 1953, deducting these sums from his gross income as ordinary and necessary business expenses (Pet. 31, R. 59). The District Court held that these payments were not ordinary and necessary business or non-business expenses of the taxpayer but were in the nature of capital investments or expenditures (R. 60–61), and the Court of Appeals affirmed (Pet. 30–37).

ARGUMENT

Upon the facts of this case the decisions of the courts below that the payments made by the taxpayer pursuant to his contract with the land owners were not deductible under Section 23(a) of the Internal Revenue Code of 1939 (Appendix, *infra*, p. 6) either as business expenses under Section 23(a)(1) or as non-business expenses under Section 23(a)(2), are correct and in accord with the statute and settled legal principles. The taxpayer urges (Pet. 20) that he was engaged in the business of managing apart-

ment buildings and that the payments in question were necessarily made for the purpose of creating a job opportunity. However, expenditures are not deductible under Section 23(a)(1) simply because they have some relation to an income-producing activity; in order to qualify, they must be incurred in the active conduct of the particular business involved. *McDonald* v. *Commissioner*, 323 U.S. 57; *Frank* v. *Commissioner*, 20 T.C. 511; *Peto* v. *Commissioner*, decided February 28, 1958 (1958 P-H T.C. Memorandum Decisions, par. 58,034), affirmed *per curiam*, 262 F. 2d 342 (C.A. 2). Obligations incurred to create a new source of income are not deductible as ordinary and necessary business expenses. *McDonald* v. *Commissioner, supra; Peto* v. *Commissioner, supra; Hammond-Knowlton* v. *Commissioner*, 19 B.T.A. 947. Cf. Treasury Regulation 118, Section 39.23(a)-15(f). Moreover, as the Court of Appeals pointed out (Pet. 34-36), the payments actually cannot be described as being predominantly for the purpose of promoting prospective employment, even if such a purpose were assumed to be sufficient for purposes of deduction. Rather, they were primarily incurred to enable the taxpayer to become the beneficial owner of an apartment "costing in the neighborhood of $2,300,000" (Pet. 35) and, in this sense, were non-deductible capital investments or expenditures. Even the taxpayer himself in his petition repeatedly states that without these payments the apartment could not have been built (Pet. 11, 12, 17).

Also, as observed by the court below (Pet. 37), the cases relied on by the taxpayer (Pet. 12-18)—*United*

States v. *E. L. Bruce Co.*, 180 F. 2d 846 (C.A. 6); *Dinardo* v. *Commissioner*, 22 T.C. 430; *Dunn & McCarthy* v. *Commissioner*, 139 F. 2d 242 (C.A. 2)—do not require a conclusion contrary to that reached by it. The present payments were not, as were the expenditures in those cases, for the protection of an existing investment or for the preservation of existing income from loss or diminution.

Further, as the Court of Appeals held (Pet. 35–36), the payments here do not qualify as "ordinary" within the meaning of Section 23(a)(1). Cf. *Welch* v. *Helvering*, 290 U.S. 111, 114; *Deputy* v. *duPont*, 308 U.S. 488, 495. For this reason, as well as for those discussed above, the taxpayer is likewise precluded from deducting the payments as non-business expenses under Section 23(a)(2). Cf. *Low* v. *Nunan*, 154 F. 2d 261 (C.A. 2). There is no conflict of decisions, and no question warranting review by this Court is presented.

CONCLUSION

The petition for writ of certiorari should be denied.

Respectfully submitted.

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DECEMBER 1959.

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*The record fails to show that the taxpayer's payments were in any way related to his continuation as manager.

APPENDIX

Internal Revenue Code of 1939:

SEC. 23 [as amended by Sec. 121(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798].
DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) *Expenses.*—

(1) *Trade or business expenses.*—

(A) *In general.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

* * * * *

(2) *Non-trade or non-business expenses.*—In the case of an individual, all the ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income.

* * * * *

(26 U.S.C. 1952 ed., 23(a).)

U. S. GOVERNMENT PRINTING OFFICE: 1959